



STATE OF NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT OF

CAPE FEAR COMMUNITY COLLEGE

WILMINGTON, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2005

OFFICE OF THE STATE AUDITOR

LESLIE W. MERRITT, JR., CPA, CFP

STATE AUDITOR

FINANCIAL STATEMENT AUDIT REPORT OF

CAPE FEAR COMMUNITY COLLEGE

WILMINGTON, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2005

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THE NORTH CAROLINA COMMUNITY COLLEGE SYSTEM

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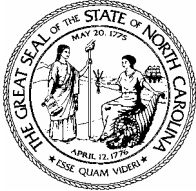
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Leslie W. Merritt, Jr., CPA, CFP
State Auditor

STATE OF NORTH CAROLINA
Office of the State Auditor

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AUDITOR'S TRANSMITTAL

The Honorable Michael F. Easley, Governor
The General Assembly of North Carolina
Board of Trustees, Cape Fear Community College

We have completed a financial statement audit of Cape Fear Community College for the year ended June 30, 2005, and our audit results are included in this report. You will note from the independent auditor's report that we determined that the financial statements are presented fairly in all material respects.

Our consideration of internal control over financial reporting and compliance and other matters based on an audit of the financial statements disclosed a deficiency that is detailed in the Audit Findings and Recommendations section of this report. The College's response is included following the finding.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

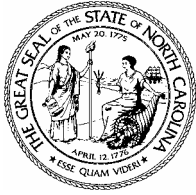
Leslie W. Merritt, Jr.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

April 5, 2006

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Cape Fear Community College
Wilmington, North Carolina

We have audited the accompanying basic financial statements of Cape Fear Community College, a component unit of the State of North Carolina, as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of the College's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Cape Fear Community College as of June 30, 2005, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 15 to the financial statements, the College implemented Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*, during the year ended June 30, 2005.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 28, 2006, on our consideration of the College's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Leslie W. Merritt, Jr.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

February 28, 2006

CAPE FEAR COMMUNITY COLLEGE MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the Cape Fear Community College annual financial report presents Management's Discussion and Analysis of the financial performance of the College during the fiscal year which ended June 30, 2005. This discussion should be read in conjunction with the accompanying financial statements and notes.

Using the Annual Financial Report

The annual report consists of financial statements, prepared in accordance with Governmental Accounting Standards Board (GASB) Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*. The financial statements focus on the financial condition of the College, the results of operations, and cash flows of the College as a whole.

The financial statements prescribed by GASB Statement No. 35 present financial information in a form similar to that used by corporations. They are prepared under the accrual basis of accounting, whereby revenues and assets are recognized when earned and expenses and liabilities are recognized when an obligation has been incurred, regardless of when cash is exchanged.

The College's net assets are one indicator of its financial stability. The Statement of Net Assets includes all assets and liabilities. The increase or decrease in net assets is an indicator of the improvement or erosion of the College's financial condition.

The Statement of Revenues, Expenses, and Changes in Net Assets presents the revenues earned and expenses incurred during the fiscal year. Activities are reported as operating or nonoperating. A college's dependency on State aid and gifts could result in operating deficits because the financial reporting model classifies State Appropriations and gifts as nonoperating revenues. The utilization of capital assets is reflected in the financial statements as depreciation.

The Statement of Cash Flows presents information related to cash inflows and outflows summarized by operating, noncapital financing, and related investing activities. The direct method is used to present cash flow.

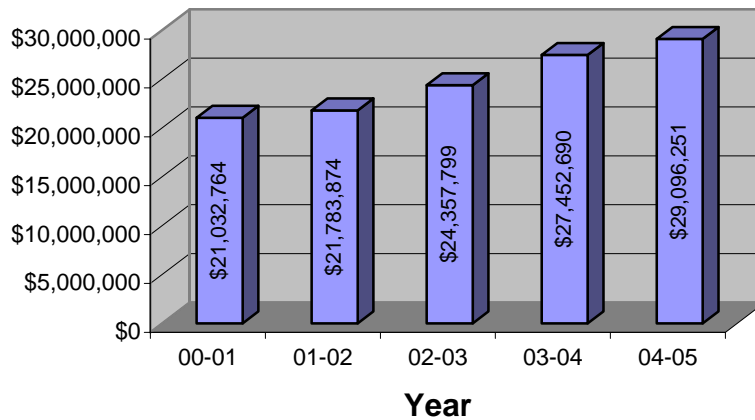
The Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

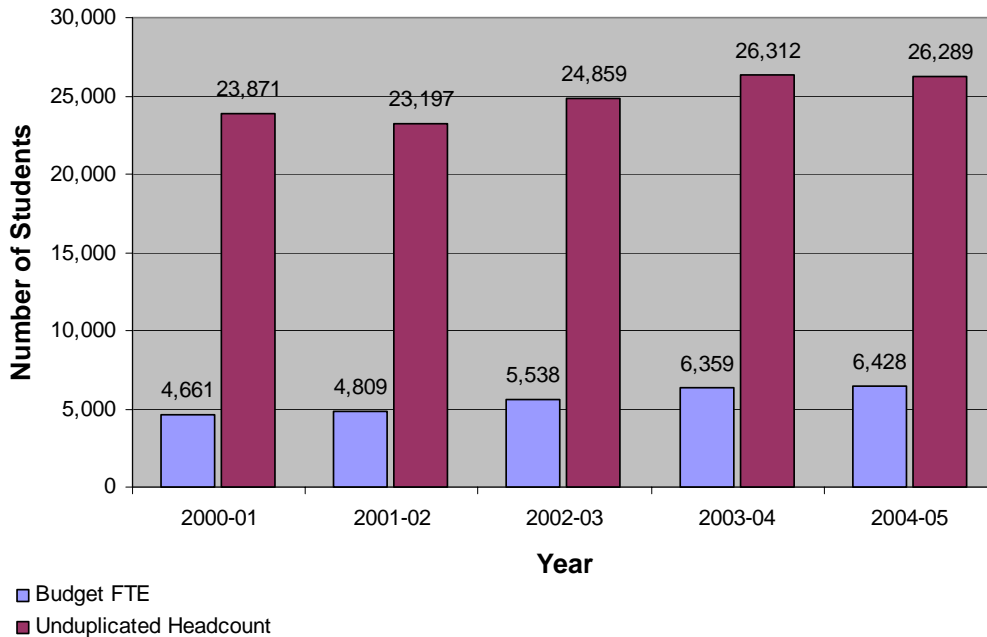
Financial Highlights

The College continues to grow by budget increases, campus expansion, and student enrollment. The budget FTE (full-time equivalency) increased by a modest 69 FTE and the unduplicated headcount decreased by 23 FTE during 2004-05. The annual appropriations however increased by \$1.60 million (6%) due to funding received for multi campus and salary increases. The State again suffered a revenue shortfall and all community colleges were mandated to revert 1.8% during the fiscal year. The College's share was \$382,000.

State Appropriations



Enrollment



MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

In addition to the funding received from the State based on FTE's, the College received \$4,738,256 from New Hanover County for the maintenance of buildings and infrastructure. The College also received \$120,000 from Pender County for operational expenses of the Burgaw and Hampstead Campuses.

The College is almost at the end of the second phase of implementing the Colleague Computer Information System (CIS) after having successfully completed the first phase. On July 1, 2005, the Student module was successfully converted to Datatel. The CIS project is the community college-wide system being implemented across the State, and the College is considered a Phase IIA site.

Financial Analysis

Statement of Net Assets

The Statement of Net Assets presents the assets (current and noncurrent), liabilities (current and noncurrent), and net assets (total assets minus total liabilities) of the College. This statement provides a fiscal snapshot of the College's financial position as of June 30, 2005. The data provides readers of this statement information on assets available to continue operations; pay amounts due vendors and lending institutions; and the net assets available for expenditure by the College. The College's net assets increased by \$2.43 million (2.9%) during fiscal year 2005.

Condensed Statement of Net Assets June 30, as Indicated

	<u>2005</u>	<u>2004</u>	<u>Change</u>	<u>% Change</u>
Assets				
Current Assets	\$ 4,979,578	\$ 4,369,564	\$ 610,014	14.0 %
Noncurrent Assets	<u>84,155,924</u>	<u>82,049,089</u>	<u>2,106,835</u>	2.6 %
Total Assets	<u><u>89,135,502</u></u>	<u><u>86,418,653</u></u>	<u><u>2,716,849</u></u>	3.1 %
Liabilities				
Current Liabilities	2,533,844	2,115,539	418,305	19.8 %
Noncurrent Liabilities	<u>1,515,645</u>	<u>1,652,706</u>	<u>(137,061)</u>	(8.3) %
Total Liabilities	<u><u>4,049,489</u></u>	<u><u>3,768,245</u></u>	<u><u>281,244</u></u>	7.5 %
Net Assets				
Invested in Capital Assets	77,152,040	69,276,649	7,875,391	11.4 %
Restricted Expendable	6,928,749	11,720,232	(4,791,483)	(40.9) %
Unrestricted	<u>1,005,224</u>	<u>1,653,527</u>	<u>(648,303)</u>	(39.2) %
Total Net Assets	<u><u>\$ 85,086,013</u></u>	<u><u>\$ 82,650,408</u></u>	<u><u>\$ 2,435,605</u></u>	2.9 %

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The total assets as of June 30 are valued at \$89.13 million. The largest asset categories include the College's net investment in capital assets for land, buildings, infrastructure, equipment, and construction-in-progress which account for 87% of total assets.

The total liabilities are valued at \$4.05 million. The largest component is contract retainage, which accounts for 35% of the total.

Statement of Revenues, Expenses, and Changes in Net Assets

Condensed Statement of Revenues, Expenses, and Changes in Net Assets For Year Ended June 30, as Indicated

	2005	2004	Change	% Change
Operating Revenue				
Tuition and Fees, Net	\$ 6,629,236	\$ 6,672,611	\$ (43,375)	(0.7) %
Federal Grants and Contracts	5,959,472	6,142,964	(183,492)	(3.0) %
State and Local Grants and Contracts	526,338	434,196	92,142	21.2 %
Sales and Services, Net	2,781,145	1,932,980	848,165	43.9 %
Other Operating Revenues	102,357	81,310	21,047	25.9 %
Total Operating Revenues	<u>15,998,548</u>	<u>15,264,061</u>	<u>734,487</u>	4.8 %
Less Operating Expenses	<u>46,494,152</u>	<u>41,070,438</u>	<u>5,423,714</u>	13.2 %
Operating Loss	<u>(30,495,604)</u>	<u>(25,806,377)</u>	<u>(4,689,227)</u>	18.2 %
Nonoperating Revenues (Expenses)				
State Aid	21,403,150	19,993,304	1,409,846	7.1 %
County Appropriations	4,345,755	3,945,280	400,475	10.2 %
Noncapital Grants	342,076	380,388	(38,312)	(10.1) %
Noncapital Gifts	247,359	349,873	(102,514)	(29.3) %
Investment Income	90,945	69,181	21,764	31.5 %
Other Nonoperating Expenses	(32,313)		(32,313)	
Other Revenues				
State Capital Aid	5,829,453	13,223,412	(7,393,959)	(55.9) %
County Capital Appropriations	499,001	290,129	208,872	72.0 %
Capital Grants	205,783	191,021	14,762	7.7 %
Total Nonoperating Revenues	<u>32,931,209</u>	<u>38,442,588</u>	<u>(5,511,379)</u>	(14.3) %
Increase in Net Assets	<u>2,435,605</u>	<u>12,636,211</u>	<u>(10,200,606)</u>	(80.7) %
Net Assets - Beginning of year	<u>82,650,408</u>	<u>70,014,197</u>	<u>12,636,211</u>	18.0 %
Net Assets - End of Year	<u>\$ 85,086,013</u>	<u>\$ 82,650,408</u>	<u>\$ 2,435,605</u>	2.9 %

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

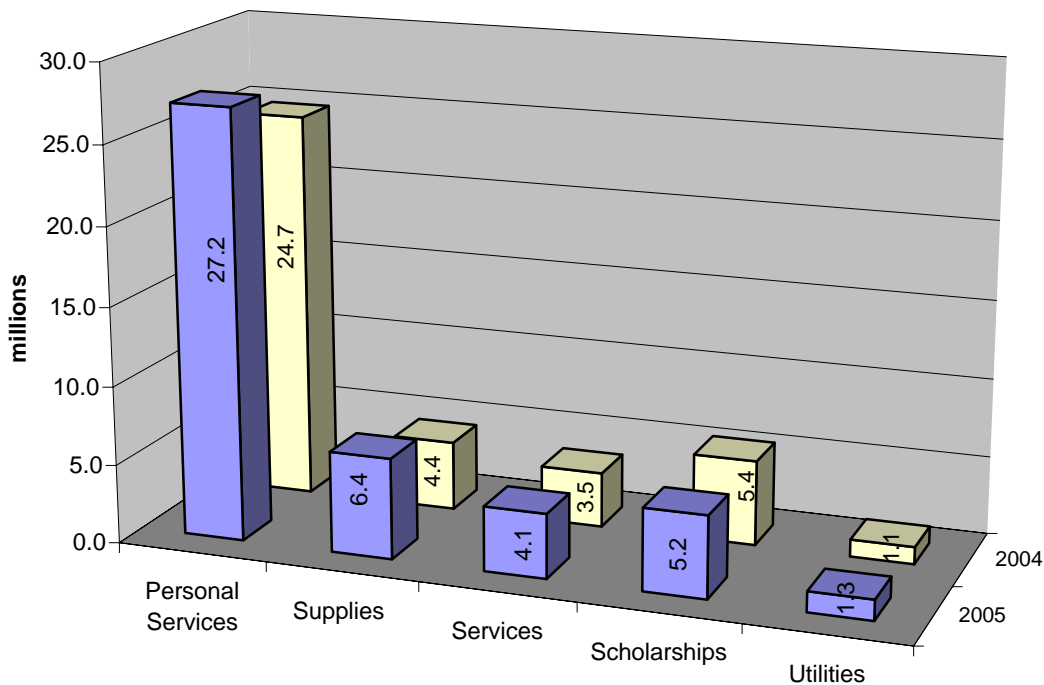
Changes in total net assets as presented on the Statement of Net Assets section are based on the activity reported in the Statement of Revenues, Expenses, and Changes in Net Assets. The purpose of this statement is to present the revenues received by the College, both operating and nonoperating, and the expenses paid by the College, operating and nonoperating, as well as any other revenues, expenses, gains and losses received or expended by the College.

Operating revenues are received for providing goods and services to the various customers and constituencies of the College. Operating expenses are used to acquire or produce the goods and services provided in return for the operating revenues, and to carry out the mission of the College. Nonoperating revenues are revenues received for which goods and services are not provided; i.e., State appropriations and investment income. Nonoperating expenses include expenses not involved in the normal operations of the College.

The total operating revenues increased by 4.8%. The majority of the revenue increase was generated by the Bookstore operations.

The nonoperating revenues (expenses) decreased by 14.3%. The majority of the decrease was contributed by State Capital Aid (55.9%) due to the completion of the Applied Technologies Building at North Campus and the resulting reduction in reimbursements for construction projects.

Operational Expenses



MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

There was an increase of \$5.40 million in operating expenses during the year. The two main components that contributed to this increase were personnel expenses of \$2.49 million due to hiring new full-time and part-time employees and secondly, supplies and material expenses of \$1.97 million due to equipping the new Applied Technologies Building at the North Campus during the fiscal year.

Statement of Cash Flows

The Statement of Cash Flows provides information about cash receipts and cash payments during the year. The Statement of Cash Flows also helps users assess the College's:

- Ability to generate future net cash flows,
- Ability to meet its obligations as they come due, and
- Need for external financing.

Condensed Statements of Cash Flows For Year Ended June 30, as Indicated

	<u>2005</u>	<u>2004</u>	<u>Change</u>	<u>% Change</u>
Cash Provided (Used) by:				
Operating Activities	\$ (28,295,165)	\$ (24,539,051)	\$ (3,756,114)	15.0 %
Noncapital Financing Activities	26,338,339	26,498,608	(160,269)	(1.0) %
Capital Financing Activities	2,234,306	(2,338,054)	4,572,360	(196.0) %
Investing Activities	90,945	69,181	21,764	31.0 %
Net Change in Cash	<u>368,425</u>	<u>(309,316)</u>	<u>677,741</u>	<u>(219.0) %</u>
Cash, Beginning of Year	<u>3,364,373</u>	<u>3,673,688</u>	<u>(309,315)</u>	<u>(8.0) %</u>
Cash, Ending of Year	<u>\$ 3,732,798</u>	<u>\$ 3,364,372</u>	<u>\$ 368,426</u>	<u>11.0 %</u>

Major sources of funds for the operating activities were provided by student tuition and fees (\$6.63 million), federal grants and contracts (\$5.96 million), and auxiliary enterprises (\$2.78 million).

Major uses of funds in operating activities were for employee compensation (\$27.18 million), payments to suppliers (\$6.36 million), scholarships (\$5.22 million), and services (\$4.12 million).

The largest inflow of funds used in operations is the appropriations from the State of North Carolina (\$21.40 million), but it is shown as nonoperating revenue per GASB 35. County appropriations inflows amounted to \$4.35 million.

The State of North Carolina also provided \$5.83 million for construction.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED)

Capital Assets

The College had \$77.26 million invested in capital assets, net of depreciation as of June 30, 2005.

Capital Assets
For the Year Ended June 30, as Indicated
(Net of Depreciation)

	<u>2005</u>	<u>2004</u>	<u>Variance</u>
Land	\$ 8,109,491	\$ 8,109,491	\$ 0.00
Construction in Progress	14,929,173	5,662,689	9,266,484
Building	48,465,606	49,667,117	(1,201,511)
Machinery and Equipment	3,362,592	3,478,489	(115,897)
Infrastructure	2,394,628	2,517,057	(122,429)
Total Capital Assets	<u>\$ 77,261,490</u>	<u>\$ 69,434,843</u>	<u>\$ 7,826,647</u>

The construction of the Applied Technologies Building, a \$16.80 million project, which began in March 2004, was completed in time for the Fall classes of 2005. Future capital projects include renovating the Emmart Building, Burnett Building, and Machine Shop by October 2005, construction of a Truck Driver Training Facility by July 2006, and a Public Safety Training Center by March 2007. During the year, the College agreed to exchange 3.5 acres of the College's property for four acres of the City of Wilmington's property in the downtown area, which will be beneficial to both parties. A study has commenced to determine the feasibility of converting the Wilmington Police Headquarters, which was part of the exchange, for the College's use. The 2000 State Bond Referendum as authorized by Senate Bill 912 will fund these projects.

Economic Forecast

Southeastern North Carolina is one of the fastest-growing areas in the country. As one of the primary providers of higher education and career training for citizens of New Hanover and Pender counties, Cape Fear Community College is one of the fastest growing community colleges in the State. To keep up with the ever-growing need for additional programs, services and classes, Cape Fear Community College has developed a plan to renovate, rebuild and construct new facilities to serve the increasing needs of local citizens, businesses, health care providers, and new and expanding industries.

Cape Fear Community College is well positioned to meet the needs of the growing community with over 60 excellent programs of study. The College constantly monitors the changes in technology and the economy and respond to the job training needs of the region. Cape Fear Community College relies on over 80 advisory committees representing over 200 area businesses to assure that the College's materials and curriculum are relevant to industry needs.

Overall, the future looks bright for Wilmington and Cape Fear Community College.

Cape Fear Community College
Statement of Net Assets
June 30, 2005

Exhibit A-1

ASSETS

Current Assets:

Cash and Cash Equivalents	\$ 795,741.06
Restricted Cash and Cash Equivalents	2,282,216.25
Receivables (Note 3)	878,711.47
Inventories	848,533.25
Prepaid Items	172,240.98
Notes Receivable (Note 3)	2,135.33
	<hr/>
Total Current Assets	4,979,578.34

Noncurrent Assets:

Restricted Cash and Cash Equivalents	654,840.33
Restricted Due from Primary Government	6,239,594.75
Capital Assets - Nondepreciable (Note 4)	23,038,663.80
Capital Assets - Depreciable, Net (Note 4)	54,222,825.20
	<hr/>
Total Noncurrent Assets	84,155,924.08
	<hr/>
Total Assets	89,135,502.42

LIABILITIES

Current Liabilities:

Accounts Payable and Accrued Liabilities (Note 5)	2,363,316.87
Deferred Revenue	27,093.39
Long-Term Liabilities - Current Portion (Note 6)	143,433.92
	<hr/>
Total Current Liabilities	2,533,844.18

Noncurrent Liabilities:

Funds Held for Others	654,840.33
Long-Term Liabilities (Note 6)	860,804.46
	<hr/>
Total Noncurrent Liabilities	1,515,644.79
	<hr/>
Total Liabilities	4,049,488.97

NET ASSETS

Invested in Capital Assets, Net of Related Debt	77,152,040.43
Restricted for Expendable:	
Loans	2,260.48
Capital Projects	6,775,499.31
Other	150,989.28
Unrestricted	1,005,223.95
	<hr/>
Total Net Assets	\$ 85,086,013.45

The accompanying notes to the financial statements are an integral part of this statement.

***Cape Fear Community College
Statement of Revenues, Expenses, and
Changes in Net Assets
For the Fiscal Year Ended June 30, 2005***

Exhibit A-2

REVENUES

Operating Revenues:

Student Tuition and Fees, Net (Note 8)	\$ 6,629,236.44
Federal Grants and Contracts	5,959,471.77
State and Local Grants and Contracts	526,338.43
Sales and Services, Net (Note 8)	2,781,144.77
Other Operating Revenues	102,357.01
	<hr/>
Total Operating Revenues	15,998,548.42

EXPENSES

Operating Expenses:

Personal Services	27,184,579.22
Supplies and Materials	6,352,173.58
Services	4,122,623.39
Scholarships and Fellowships	5,215,457.69
Utilities	1,327,319.66
Depreciation	2,291,998.48
	<hr/>
Total Operating Expenses	46,494,152.02

Operating Loss (30,495,603.60)

NONOPERATING REVENUES (EXPENSES)

State Aid	21,403,150.16
County Appropriations	4,345,755.00
Noncapital Grants	342,075.66
Noncapital Gifts	247,358.58
Investment Income	90,944.92
Other Nonoperating Expenses	(32,313.12)
	<hr/>
Net Nonoperating Revenues	26,396,971.20

Loss Before Other Revenues (4,098,632.40)

State Capital Aid	5,829,453.62
County Capital Appropriations	499,001.00
Capital Grants	205,783.04
	<hr/>

Increase in Net Assets 2,435,605.26

NET ASSETS

Net Assets, July 1, 2004	<u>82,650,408.19</u>
Net Assets, June 30, 2005	<u><u>\$ 85,086,013.45</u></u>

The accompanying notes to the financial statements are an integral part of this statement.

***Cape Fear Community College
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2005***

Exhibit A-3

CASH FLOWS FROM OPERATING ACTIVITIES

Received from Customers	\$ 15,966,767.01
Payments to Employees and Fringe Benefits	(27,022,262.88)
Payments to Vendors and Suppliers	(12,155,256.78)
Payments for Scholarships and Fellowships	(4,986,261.68)
Loans Issued to Students	(316.41)
Other Payments	(97,834.41)
	<u>(97,834.41)</u>
Net Cash Used by Operating Activities	<u>(28,295,165.15)</u>

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

State Aid Received	21,403,150.16
County Appropriations	4,345,755.00
Noncapital Grants Received	342,075.66
Noncapital Gifts Received	247,358.58
	<u>247,358.58</u>
Cash Provided by Noncapital Financing Activities	<u>26,338,339.40</u>

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES

State Capital Aid Received	11,461,696.99
County Capital Appropriations	499,001.00
Capital Grants Received	205,783.04
Acquisition and Construction of Capital Assets	(9,883,429.96)
Principal Paid on Capital Debt and Leases	(48,745.53)
	<u>(48,745.53)</u>
Net Cash Provided by Capital and Related Financing Activities	<u>2,234,305.54</u>

CASH FLOWS FROM INVESTING ACTIVITIES

Investment Income	<u>90,944.92</u>
Cash Provided by Investing Activities	<u>90,944.92</u>

Net Increase in Cash and Cash Equivalents	368,424.71
Cash and Cash Equivalents, July 1, 2004	<u>3,364,372.93</u>
Cash and Cash Equivalents, June 30, 2005	<u><u>\$ 3,732,797.64</u></u>

**RECONCILIATION OF OPERATING LOSS
TO NET CASH USED BY OPERATING ACTIVITIES**

Operating Loss	\$ (30,495,603.60)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:	
Depreciation Expense	2,291,998.48
Changes in Assets and Liabilities:	
Receivables	197,718.90
Inventories	(280,880.27)
Prepaid Items	(70,544.33)
Notes Receivable	(316.41)
Accounts Payable and Accrued Liabilities	103,378.19
Deferred Revenue	(7,286.35)
Funds Held for Others	(92,567.91)
Compensated Absences	58,938.15
	<u>58,938.15</u>
Net Cash Used by Operating Activities	<u><u>\$ (28,295,165.15)</u></u>

***Cape Fear Community College
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2005***

Exhibit A-3

Page 2

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:	
Cash and Cash Equivalents	\$ 795,741.06
Restricted Cash and Cash Equivalents	2,282,216.25
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	<u>654,840.33</u>
Total Cash and Cash Equivalents - June 30, 2005	<u>\$ 3,732,797.64</u>

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Assets Acquired Through the Assumption of a Liability	\$ 267,527.81
Capital Asset Write-Offs	69,837.36

The accompanying notes to the financial statements are an integral part of this statement.

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CAPE FEAR COMMUNITY COLLEGE
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2005

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

- A. Financial Reporting Entity** - The concept underlying the definition of the financial reporting entity is that elected officials are accountable to their constituents for their actions. As required by accounting principles generally accepted in the United States of America, the financial reporting entity includes both the primary government and all of its component units. An organization other than a primary government serves as a nucleus for a reporting entity when it issues separate financial statements. Cape Fear Community College is a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report*.

The accompanying financial statements present all funds for which the College's Board of Trustees is financially accountable. Related foundations and similar nonprofit corporations for which the College is not financially accountable or for which the nature of their relationship is not considered significant to the College are not part of the accompanying financial statements.

- B. Basis of Presentation** - The accompanying financial statements are presented in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

Pursuant to the provisions of GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, the full scope of the College's activities is considered to be a single business-type activity and accordingly, is reported within a single column in the basic financial statements.

In accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the College does not apply Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, for proprietary activities, unless the GASB amends its pronouncements to specifically adopt FASB pronouncements issued after that date.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

- C. Basis of Accounting** - The financial statements of the College have been prepared using the economic resource measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.
- D. Cash and Cash Equivalents** - This classification includes undeposited receipts, petty cash, cash on deposit with private bank accounts, and deposits held by the State Treasurer in the short-term investment portfolio. The short-term investment portfolio maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.
- E. Receivables** - Receivables consist of tuition and fees charged to students and charges for auxiliary enterprises' sales and services. Receivables also include amounts due from the federal government, State and local governments, and private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants. Receivables are shown at book value with no provision for doubtful accounts considered necessary.
- F. Inventories** - Inventories, consisting of expendable supplies, are valued at cost using the first-in, first-out method.
- G. Capital Assets** - Capital assets are stated at cost at date of acquisition or fair value at date of donation in the case of gifts. The College capitalizes assets that have a value or cost in excess of \$5,000 at the date of acquisition and an expected useful life of more than one year. Library books are generally not considered to have a useful life of more than one year unless part of a collection and are expensed in the year of acquisition.

Depreciation is computed using the straight-line and/or units of output method over the estimated useful lives of the assets, generally 15 to 25 years for general infrastructure, 20 to 40 years for buildings, and 5 to 15 years for equipment.

- H. Restricted Assets** - Unexpended capital contributions are classified as restricted assets because their use is limited by donor/grantor agreements. Certain other assets are classified as restricted because their use is limited by external parties or statute.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

- I. Noncurrent Long-Term Liabilities** - Noncurrent long-term liabilities include notes payable and compensated absences that will not be paid within the next fiscal year.
- J. Compensated Absences** - The College's policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1 or for which an employee can be paid upon termination of employment. Also, any accumulated vacation leave in excess of 30 days at year end is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30 equals the leave carried forward at the previous December 31 plus the leave earned, less the leave taken between January 1 and June 30.

In addition to the vacation leave described above, compensated absences includes the accumulated unused portion of the special annual leave bonuses awarded by the College to all full-time permanent employees as of September 30, 2002, and as of July 1, 2003. The unused portion of this leave remains available until used, notwithstanding the limitation on annual leave carried forward described above.

When classifying compensated absences into current and noncurrent, leave is considered taken using the last-in, first-out method.

- K. Net Assets** - The College's net assets are classified as follows:

Invested in Capital Assets, Net of Related Debt - This represents the College's total investment in capital assets, net of outstanding debt obligations related to those capital assets.

Restricted Net Assets – Expendable - Expendable restricted net assets include resources for which the College is legally or contractually obligated to spend in accordance with restrictions imposed by external parties.

Unrestricted Net Assets - Unrestricted net assets include resources derived from student tuition and fees, sales and services, unrestricted gifts, and interest income.

Restricted and unrestricted resources are tracked using a fund accounting system and are spent in accordance with established fund authorities. Fund authorities provide rules for the fund activity and are separately established for restricted and unrestricted activities. When both restricted and unrestricted funds are available for expenditure, the decision for funding is transactional based within the departmental management system in place at the College.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

- L. Scholarship Discounts** - Student tuition and fees revenues and certain other revenues from College charges are reported net of scholarship discounts in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. The scholarship discount is the difference between the actual charge for goods and services provided by the College and the amount that is paid by students or by third parties on the students' behalf. Student financial assistance grants, such as Pell grants, and other federal, State, or nongovernmental programs, are recorded as either operating or nonoperating revenues in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. To the extent that revenues from these programs are used to satisfy tuition, fees, and other charges, the College has recorded a scholarship discount.
- M. Revenue and Expense Recognition** - The College classifies its revenues and expenses as operating or nonoperating in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the College's principal ongoing operations. Operating revenues include activities that have characteristics of exchange transactions, such as (1) student tuition and fees, (2) sales and services of auxiliary enterprises, and (3) certain federal, State and local grants and contracts. Operating expenses are all expense transactions incurred other than those related to capital and noncapital financing or investing activities as defined by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*.
- Nonoperating revenues include activities that have the characteristics of nonexchange transactions. Revenues from nonexchange transactions and State aid that represent subsidies or gifts to the College, as well as investment income, are considered nonoperating since these are either investing, capital or noncapital financing activities. Capital contributions are presented separately after nonoperating revenues and expenses.
- N. County Appropriations** - County appropriations are provided to the College primarily to fund its plant operation and maintenance function and to fund construction projects, motor vehicle purchases, and maintenance of equipment. Unexpended county current appropriation and county capital appropriation do not revert and are available for future use by the College.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 2 - DEPOSITS

All funds of the College are deposited in board-designated official depositories and are required to be collateralized in accordance *General Statute* 115D-58.7. Official depositories may be established with any bank or savings and loan association whose principal office is located in North Carolina. Also, the College may establish time deposit accounts, money market accounts, and certificates of deposit. The amount shown on the Statement of Net Assets as cash and cash equivalents includes cash on hand totaling \$13,410.00 and deposits in private financial institutions with a carrying value of \$385,836.74 and a bank balance of \$759,916.89.

The North Carolina Administrative Code (20 NCAC 7) requires all depositories to collateralize public deposits in excess of federal depository insurance coverage by using one of two methods, dedicated or pooled. Under the dedicated method, a separate escrow account is established by each depository in the name of each local governmental unit and the responsibility of monitoring collateralization rests with the local unit. Under the pooling method, each depository establishes an escrow account in the name of the State Treasurer to secure all of its public deposits. This method shifts the monitoring responsibility from the local unit to the State Treasurer.

Custodial credit risk is the risk that in the event of a bank failure, the College's deposits may not be returned to it. As of June 30, 2005, the College's bank balance in excess of federal depository insurance coverage was covered under the pooling method.

The College is authorized to invest idle funds as provided by G.S. 115D-58.6. In accordance with this statute, the College and the Board of Trustees manage investments to ensure they can be converted into cash when needed.

Generally, funds belonging to the College may be invested in the form of investments pursuant to G.S. 159-30(c), as follows: a commingled investment pool established and administered by the State Treasurer pursuant to G.S. 147-69.3, obligations of or fully guaranteed by the United States; obligations of the State of North Carolina; bonds and notes of any North Carolina local government or public authority; obligations of certain nonguaranteed federal agencies; prime quality commercial paper bearing specified ratings and banker's acceptances; The North Carolina Capital Management Trust, an SEC registered mutual fund; repurchase agreements; and evidences of ownership of, or fractional undivided interests in, future interest and principal payments on either direct obligations of or fully guaranteed by the United States government, which are held by a specified bank or trust company or any state in the capacity.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

At June 30, 2005, the amount shown on the Statement of Net Assets as cash and cash equivalents includes \$3,333,550.90 which represents the College's equity position in the State Treasurer's Short-Term Investment Fund. The Short-Term Investment Fund (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 1.41 years as of June 30, 2005. Assets and shares of the Short-Term Investment Fund are valued at amortized cost, which approximates fair value. Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's Short-Term Investment Fund) are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.ncosc.net/> and clicking on "Financial Reports", or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

NOTE 3 - RECEIVABLES

Receivables at June 30, 2005, were as follows:

	<u>Amount</u>
Current Receivables:	
Students	\$ 237,365.14
Accounts	65,170.56
Intergovernmental	559,373.86
Other	<u>16,801.91</u>
Total Current Receivables	<u>\$ 878,711.47</u>
Notes Receivable - Current:	
Institutional Student Loan Programs	<u>\$ 2,135.33</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 4 - CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2005, is presented as follows:

	Balance July 1, 2004	Increases	Decreases	Balance June 30, 2005
Capital Assets, Nondepreciable:				
Land	\$ 8,109,491.04	\$ 0.00	\$ 0.00	\$ 8,109,491.04
Construction in Progress	5,662,689.05	9,266,483.71		14,929,172.76
Total Capital Assets, Nondepreciable	13,772,180.09	9,266,483.71		23,038,663.80
Capital Assets, Depreciable:				
Buildings	58,269,312.86	285,230.75		58,554,543.61
Machinery and Equipment	6,001,945.49	589,852.45	69,837.36	6,521,960.58
General Infrastructure	2,998,435.52	9,390.86		3,007,826.38
Total Capital Assets, Depreciable	67,269,693.87	884,474.06	69,837.36	68,084,330.57
Less Accumulated Depreciation:				
Buildings	8,602,196.47	1,486,741.55		10,088,938.02
Machinery and Equipment	2,523,455.58	673,437.25	37,524.24	3,159,368.59
General Infrastructure	481,379.08	131,819.68		613,198.76
Total Accumulated Depreciation	11,607,031.13	2,291,998.48	37,524.24	13,861,505.37
Total Capital Assets, Depreciable, Net	55,662,662.74	(1,407,524.42)	32,313.12	54,222,825.20
Capital Assets, Net	\$ 69,434,842.83	\$ 7,858,959.29	\$ 32,313.12	\$ 77,261,489.00

NOTE 5 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2005, were as follows:

	Amount
Accounts Payable	\$ 473,474.65
Accrued Payroll	473,211.80
Contract Retainage	1,416,630.42
Total Accounts Payable and Accrued Liabilities	\$ 2,363,316.87

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 6 - LONG-TERM LIABILITIES

A. Changes in Long-Term Liabilities - A summary of changes in the long-term liabilities is presented as follows:

	Balance July 1, 2004	Additions	Reductions	Balance June 30, 2005	Current Portion
Notes Payable	\$ 158,194.10	\$ 0.00	\$ 48,745.53	\$ 109,448.57	\$ 51,334.11
Compensated Absences	835,851.66	608,060.06	549,121.91	894,789.81	92,099.81
Total Long-Term Liabilities	\$ 994,045.76	\$ 608,060.06	\$ 597,867.44	\$ 1,004,238.38	\$ 143,433.92

B. Notes Payable - The College was indebted for notes payable for the purposes shown in the following table:

Purpose	Financial Institution	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through 06/30/2005	Principal Outstanding 06/30/2005
Telephone System	BB&T	4.18	01/31/2007	\$ 178,227.00	\$ 117,712.67	\$ 60,514.33
Point-of-Sale System	Nebraska Book Co.	8.50	01/02/2008	69,917.11	20,982.87	48,934.24
Total Notes Payable				<u>\$ 248,144.11</u>	<u>\$ 138,695.54</u>	<u>\$ 109,448.57</u>

C. Annual Requirements - The annual requirements to pay principal and interest on the notes payable at June 30, 2005, are as follows:

Fiscal Year	Annual Requirements	
	Notes Payable	
	Principal	Interest
2006	\$ 51,334.11	\$ 5,974.82
2007	37,477.49	3,325.43
2008	15,988.41	1,754.13
2009	4,648.56	394.91
Total Requirements	<u>\$ 109,448.57</u>	<u>\$ 11,449.29</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 7 - OPERATING LEASE OBLIGATIONS

Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2005:

<u>Fiscal Year</u>	<u>Amount</u>
2006	\$ 94,126.45
2007	72,591.75
2008	65,391.75
2009	<u>23,895.43</u>
Total Minimum Lease Payments	<u><u>\$ 256,005.38</u></u>

Rental expense for all operating leases during the year was \$128,460.92

NOTE 8 - REVENUES

A summary of eliminations and allowances by revenue classification is presented as follows:

	<u>Gross Revenues</u>	<u>Less Scholarship Discounts</u>	<u>Net Revenues</u>
Operating Revenues:			
Student Tuition and Fees	\$ 7,893,258.99	\$ 1,264,022.55	\$ 6,629,236.44
Sales and Services:			
Sales and Services of Auxiliary Enterprises:			
Daycare	\$ 292,592.51	\$ 0.00	\$ 292,592.51
Activity Fee	170,197.37	50,206.00	119,991.37
Bookstore	2,551,863.44	420,744.63	2,131,118.81
Parking	52,906.00		52,906.00
Vending	170,722.67		170,722.67
Other	<u>13,813.41</u>		<u>13,813.41</u>
Total Sales and Services	<u><u>\$ 3,252,095.40</u></u>	<u><u>\$ 470,950.63</u></u>	<u><u>\$ 2,781,144.77</u></u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 9 - OPERATING EXPENSES BY FUNCTION

The College's operating expenses by functional classification are presented as follows:

	Personal Services	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation	Total
Instruction	\$ 17,125,572.22	\$ 2,912,364.83	\$ 933,560.02	\$ 801,563.88	\$ 0.00	\$ 0.00	\$ 21,773,060.95
Academic Support	3,155,562.49	231,042.46	235,984.54				3,622,589.49
Student Services	1,754,240.39	179,164.72	272,553.10	431,557.98			2,637,516.19
Institutional Support	3,702,577.29	129,081.45	1,162,350.88				4,994,009.62
Operations and Maintenance of Plant	1,052,670.65	814,113.17	1,144,901.99		1,327,319.66		4,339,005.47
Student Financial Aid			8,067.59	3,982,335.83			3,990,403.42
Auxiliary Enterprises	393,956.18	2,086,406.95	365,205.27				2,845,568.40
Depreciation						2,291,998.48	2,291,998.48
	<u>\$ 27,184,579.22</u>	<u>\$ 6,352,173.58</u>	<u>\$ 4,122,623.39</u>	<u>\$ 5,215,457.69</u>	<u>\$ 1,327,319.66</u>	<u>\$ 2,291,998.48</u>	<u>\$ 46,494,152.02</u>

NOTE 10 - PENSION PLANS

A. Retirement Plans - Each permanent full-time employee, as a condition of employment, is a member of the Teachers' and State Employees' Retirement System. The Teachers' and State Employees' Retirement System (System) is a cost sharing multiple-employer defined benefit pension plan administered by the North Carolina State Treasurer.

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by *North Carolina General Statutes* 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 2005, these rates were set at 2.17% of covered payroll for employers and 6% of covered payroll for members.

For the year ended June 30, 2005, the College had a total payroll of \$22,954,703.09, of which \$18,260,175.85 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were \$1,095,610.55 and \$396,245.82, respectively. The College made 100% of its annual required contributions for the years ended June 30, 2005, 2004, and 2003, which were \$396,245.82, \$36,330.32, and \$0.00, respectively.

The Teachers' and State Employees' Retirement System's financial information is included in the State of North Carolina's *Comprehensive*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Annual Financial Report. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.ncosc.netstate.nc.us/> and clicking on "Financial Reports", or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

- B. Deferred Compensation and Supplemental Retirement Income Plans** - IRC Section 457 Plan - The State of North Carolina offers its permanent employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457 through the North Carolina Public Employee Deferred Compensation Plan (the Plan). The Plan permits each participating employee to defer a portion of his or her salary until future years. The deferred compensation is available to employees upon separation from service, death, disability, retirement, or financial hardships if approved by the Board of Trustees of the Plan. The Board, a part of the North Carolina Department of Administration, maintains a separate fund for the exclusive benefit of the participating employees and their beneficiaries, *the North Carolina Public Employee Deferred Compensation Trust Fund*. The Board also contracts with an external third party to perform certain administrative requirements and to manage the trust fund's assets. All costs of administering and funding the Plan are the responsibility of the Plan participants. No costs are incurred by the College. The voluntary contributions by employees amounted to \$37,822.20 for the year ended June 30, 2005.

IRC Section 401(k) Plan - All members of the Teachers' and State Employees' Retirement System are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the Plan are the responsibility of the Plan participants. No costs are incurred by the College. The voluntary contributions by employees amounted to \$274,389.34 for the year ended June 30, 2005.

IRC Section 403(b) and 403(b)(7) Plans - Eligible College employees can participate in tax sheltered annuity plans created under Internal Revenue Code Sections 403(b) and 403(b)(7). The employee's eligible contributions, made through salary reduction agreements, are exempt from federal and State income taxes until the annuity is received or the contributions are withdrawn. These plans are exclusively for employees of colleges and certain charitable and other nonprofit institutions. All costs of administering and funding these plans are the responsibility of the Plan participants. No costs are incurred by the College. The voluntary contributions by employees amounted to \$119,596.16 for the year ended June 30, 2005.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 11 - OTHER POSTEMPLOYMENT BENEFITS

- A. Health Care for Long-Term Disability Beneficiaries and Retirees -** The College participates in State-administered programs which provide post employment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System. These benefits were established by Chapter 135, Article 3, Part 3, of the General Statutes and may be amended only by the North Carolina General Assembly. Funding for the health care benefit for long-term disability beneficiaries and retirees is financed on a pay-as-you-go basis. The College contributed 3.2% of the covered payroll under the Teachers' and State Employees' Retirement System for these health care benefits. For the fiscal year ended June 30, 2005, the College's total contribution to the Plan was \$584,325.63. The College assumes no liability for retiree health care benefits provided by the programs other than its required contribution. Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*.
- B. Long-Term Disability -** The College participates in the Disability Income Plan of North Carolina (DIPNC). Established by Chapter 135, Article 6, of the General Statutes, DIPNC provides short-term and long-term disability benefits to eligible members of the Teachers' and State Employees' Retirement System. Long-term disability income benefits are advance funded on an actuarially determined basis using the one-year term cost method. Employer contributions are established in the Appropriations Bill by the General Assembly. The College contributes .445% of covered payroll under the Teachers' and State Employees' Retirement System to the DIPNC. For the year ended June 30, 2005, the College's total contribution to the DIPNC was \$81,257.78. The College assumes no liability for long-term disability benefits under the Plan other than its contribution. Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*.

NOTE 12 - RISK MANAGEMENT

The College is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These exposures to loss are handled via a combination of methods, and can include participation in State-administered insurance programs, purchase of commercial insurance, and self-retention of certain risks. There have been no significant reductions in insurance coverage from

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

Tort claims of up to \$500,000 are self-insured under the authority of the State Tort Claims Act. In addition, the State provides excess public officers' and employees' liability insurance up to \$5 million via contract with a private insurance company. The premium, based on a composite rate, is paid by the North Carolina Community College System Office directly to the private insurer.

Fire and other property losses are covered by the Public School Insurance Fund, a State-administered public entity risk pool. This fund is financed by premiums and interest and incurs a \$10 million self-insured deductible per occurrence. Reinsurance is purchased by the fund to cover catastrophic events in excess of the \$10 million deductible. There have been no significant reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

State-owned vehicles used for instructional purposes are covered by liability insurance handled by the State Department of Insurance. Liability insurance for other College-owned vehicles is covered by contracts with private insurance companies.

The College is protected for losses from employee dishonesty and computer fraud for employees paid in whole or in part from State funds. The blanket honesty bond is with a private insurance company and is handled by the North Carolina Department of Insurance with coverage of \$5,000,000 per occurrence and a \$50,000 deductible. The College purchases coverage for losses from employee dishonesty for county and institutional fund paid employees under an employee dishonesty bond.

The College purchased other authorized coverage from private insurance companies through the North Carolina Department of Insurance. Other insurance purchased by the College included day care general liability with coverage of \$1,000,000 per occurrence and a \$1,000 deductible and flood insurance with coverage's ranging from \$500,000 to \$5,000,000 depending upon the building damaged with a \$5,000 deductible.

Employees and retirees are provided health care coverage by the Comprehensive Major Medical Plan (Plan), a component unit of the State. The Plan is funded by employer and employee contributions and is administered by a third-party contractor.

The State Board of Community Colleges makes the necessary arrangements to carry out the provisions of the Workers' Compensation Act which are applicable to employees whose wages are paid in whole or in part from State

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

funds. The College purchases workers' compensation insurance for employees whose salaries or wages are paid by the Board entirely from county or institutional funds.

Term life insurance of \$25,000 to \$50,000 is provided to eligible workers. This self-insured death benefit program is administered by the State Treasurer and funded via employer contributions. There were no employer contributions required for the current fiscal year.

Additional details on the State-administered risk management programs are disclosed in the State's *Comprehensive Annual Financial Report*, issued by the Office of the State Controller.

NOTE 13 - COMMITMENTS AND CONTINGENCIES

A. Commitments - The College has established an encumbrance system to track its outstanding commitments on construction projects and other purchases. Outstanding commitments on construction contracts were \$2,201,872.33 and on other purchases were \$1,864,458.18 at June 30, 2005.

B. Community College General Obligation Bonds - The 1999-2000 Session of the General Assembly of North Carolina authorized the issuance of \$600 million of general obligation bonds of the State, as subsequently approved by a vote of qualified voters of the State, to provide funds for capital improvements for the North Carolina Community College System. The funds authorized are to be used solely to construct new buildings and to renovate and modernize existing buildings on the North Carolina Community College System campuses. The bond legislation specifies the amount of bond funding for each College campus as well as the intended amount for new construction and repair and replacement. The legislation further provides that the State Board of Community Colleges shall be responsible for the approval of projects in accordance with provisions of the legislation. The bonds were authorized for issuance over a six-year period beginning in 2001 at a level not to exceed amounts provided in the legislation. Using a cash flow financing approach, The Community College System's Office (CCSO) establishes annual amounts not to exceed for each approved project. The amounts not to exceed are subject to change due to actual cash availability and needs during the year. Subsequent to the bond sales and the availability of bond proceeds, CCSO notifies the Office of State Budget and Management (OSBM) of the amount not to exceed for the total of the approved projects. Within this amount, based on an official request of cash needs from the State Board of Community Colleges, OSBM

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

authorizes allotments. These allotments are then recorded to specific community college allotment accounts by the CCSO. The College records the allotments as revenue on the accompanying financial statements. The College's remaining authorization of \$13,383,261.00 is contingent on future bond sales and CCSO allotment approval. Because of uncertainty and time restrictions the remaining authorization is not recorded as an asset or revenue on the accompanying financial statements.

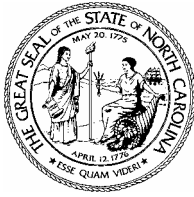
NOTE 14 - CAPE FEAR COMMUNITY COLLEGE FOUNDATION, INC.

The Cape Fear Community College Foundation, Inc. is a separately incorporated nonprofit foundation associated with the College. This organization serves as the primary fundraising arm of the College through which individuals, corporations, and other organizations support College programs by providing scholarships, fellowships, faculty salary supplements, and unrestricted funds to specific departments and the College's overall academic environment. The College's financial statements do not include the assets, liabilities, net assets, or operational transactions of the Foundation, except for the distributions made and benefits provided by the Foundation. The distributions received and/or benefits provided approximated \$100,858.30 for the year ended June 30, 2005.

NOTE 15 - CHANGE IN FINANCIAL ACCOUNTING AND REPORTING

For the fiscal year ended June 30, 2005, the College implemented Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*. This Statement establishes and modifies disclosure requirements related to investment risks: credit risk, interest rate risk, and foreign currency risk. This statement also establishes and modifies disclosure requirements for deposit risks: custodial credit risk and foreign currency risk.

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**INDEPENDENT AUDITOR'S REPORT
ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN
AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

Board of Trustees
Cape Fear Community College
Wilmington, North Carolina

We have audited the financial statements of Cape Fear Community College, a component unit of the State of North Carolina, as of and for the year ended June 30, 2005, and have issued our report thereon dated February 28, 2006.

As discussed in Note 15 to the financial statements, the College implemented Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*, during the year ended June 30, 2005.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the College's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the College's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition is described in the Audit Findings and Recommendations section of this report.

Finding

Inadequate Separation of Duties and Management Oversight

**INDEPENDENT AUDITOR'S REPORT
ON INTERNAL CONTROL OVER FINANCIAL REPORTING
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A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe the reportable condition described above is not a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the College's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Board of Trustees, the State Board of Community Colleges, management of the College, the Governor, the State Controller, the General Assembly, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor



February 28, 2006

AUDIT FINDINGS AND RECOMMENDATIONS

Matter Related to Financial Reporting

The following finding was identified during the current audit and describes a condition that represents a significant deficiency in internal control.

INADEQUATE SEPARATION OF DUTIES AND MANAGEMENT OVERSIGHT

The College did not have adequate controls in place to assure proper segregation of duties and proper review and approval procedures. The Controller reconciled all bank accounts; however, there was no further review by upper management except at June 30, 2005. Although the Controller did not have duties involving cash receipting or cash disbursements, he did have access to the general ledger which provided a means of manipulating the system via journal entry as well as access to blank check stock. Because the Controller had access to blank check stock, fraudulent checks could be created and processed outside the College's Financial System without being detected.

Recommendation: To ensure proper controls over cash receipts and disbursements, bank reconciliations should be performed on a monthly basis by an employee independent of duties involving cash processing. Management oversight should be involved in the review and approval of completed bank reconciliations.

College's Response: The task of reconciling bank statements has been assigned to the Accounting Technician. The Controller will review and approve the reconciliations as completed. Changes were made to the Controller's and Accounting Technician's access rights to Colleague. The changes prohibit them from (1) creating, modifying, and deleting vouchers; (2) creating, modifying, and voiding checks; and (3) printing checks.

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